



# STATE BOARD OF EQUALIZATION STAFF LEGISLATIVE BILL ANALYSIS

# DRAFT

Date Amended:	03/09/11	Bill No:	<a href="#">Assembly Bill 686</a>
Tax Program:	Transactions and Use	Author:	Huffman
Sponsor:	County of Marin	Code Sections:	RTC 7285, 7285.5, 7285.9, & 7285.91
Related Bills:	AB 1086 (Wieckowski)	Effective Date:	01/01/12

## BILL SUMMARY

This bill would decrease the rate at which a county or a city may levy, increase, or extend a transactions and use tax to a rate of 0.125, or multiples of 0.125 percent (currently 0.25 or multiples of 0.25 percent).

## ANALYSIS

### CURRENT LAW

The State Board of Equalization (BOE) administers local sales and use taxes under the Bradley-Burns Uniform Local Sales and Use Tax Law and under the Transactions and Use Tax Law, which are divisions of the Revenue and Taxation Code.

The **Bradley-Burns Uniform Local Sales and Use Tax Law** (commencing with Revenue and Taxation Code Section 7200) authorizes cities and counties to impose a local sales and use tax. The rate of tax is fixed at 1.25 percent of the sales price of tangible personal property sold at retail in the local jurisdiction, or purchased outside the jurisdiction for use within the jurisdiction. However, beginning July 1, 2004, and continuing through the “revenue exchange period” (also known as the “Triple Flip”), Section 7203.1 temporarily suspends the authority of a county or a city to impose a tax under Sections 7202 and 7203, and instead provides that the applicable rate is the following: (1) in the case of a county, 1 percent; and (2) in the case of a city, 0.75 percent or less. “Revenue exchange period” means the period on or after July 1, 2004, and continuing until the Department of Finance notifies the BOE, pursuant to Government Code Section 99006, that the \$15 billion Economic Recovery Bonds have been repaid or that there is sufficient revenue to satisfy the state’s bond obligations.

Of the 1 percent, cities and counties use the 0.75 percent to support general operations. The remaining 0.25 percent is designated by statute for county transportation purposes and may be used only for road maintenance or the operation of transit systems. The counties receive the 0.25 percent tax for transportation purposes regardless of whether the sale occurs in a city or in the unincorporated area of a county. All local jurisdictions impose the Bradley-Burns local taxes at the uniform rate of 1 percent.

The **Transactions and Use Tax Law** (Part 1.6, commencing with Revenue and Taxation Code Section 7251) and the Additional Local Tax Law (Part 1.7, commencing with Section 7285) authorizes cities and counties to impose transactions and use taxes (hereinafter referred to as district taxes) under specified conditions. **Section 7285** authorizes a county to impose a district tax for general purposes at a rate of 0.25 percent, or multiple thereof, if the ordinance proposing the tax is approved by a two-

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thirds vote of the board of supervisors and a majority vote of the qualified voters of the county. **Section 7285.5** authorizes a county to impose a district tax for special purposes at a rate of 0.25 percent, or multiple thereof, if the ordinance proposing the tax is approved by a two-thirds vote of the board of supervisors and a two-thirds vote of the qualified voters of the county.

For purposes of funding libraries, **Section 7286.59** authorizes a county to impose a district tax at a rate of either 0.125 or 0.25 percent for a period not to exceed 16 years, if the ordinance proposing the tax is approved by the board of supervisors and a two-thirds vote of the qualified voters of the county. The revenues are to be used exclusively for funding public library construction, acquisition, programs, and operations within the county.

With respect to cities, **Section 7285.9** authorizes a city to impose a district tax for general purposes at a rate of 0.25 percent, or multiple thereof, if the ordinance proposing the tax is approved by a two-thirds vote of all members of the governing body and a majority vote of the qualified voters of the city. **Section 7285.91** authorizes a city to impose a district tax for special purposes at a rate of 0.25 percent, or multiple thereof, if the ordinance proposing the tax is approved by a two-thirds vote of all member of the governing body and a two-thirds vote of the qualified voters of the county.

The combined rate of all district taxes imposed in any county cannot exceed 2 percent.

Cities and counties are required to contract with the BOE to perform all functions in the administration and operations of the ordinances imposing the Bradley-Burns local taxes and the district taxes.

#### PROPOSED LAW

This bill would amend Sections 7285 and 7285.5 to decrease the rate at which a county may levy, increase, or extend a transactions and use tax to 0.125, or multiples of 0.125 percent, for general and special purposes. This bill would also amend Sections 7285.9 and 7285.91 to decrease the rate at which a city may do the same.

The bill would become effective on January 1, 2012.

#### IN GENERAL

Cities and counties may impose a district tax for general or specific purposes. These taxes can be imposed either directly by the city or county or through a special purpose entity established by the city or county. Counties can also establish a transportation authority to impose district taxes under the Public Utilities Code.

Beginning April 1, 2011, there will be 132 local jurisdictions (city, county, and special purpose entity) imposing a district tax for general or specific purposes. Of the 132 jurisdictions, 40 are county-imposed taxes and 92 are city-imposed taxes.

As stated previously, the combined rate of all district taxes imposed in any county shall not exceed 2 percent. District taxes increase the tax rate within a city or county by adding the district tax rate to the combined state and local (Bradley-Burns local tax) tax rate of 8.25 percent<sup>1</sup>.

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<sup>1</sup>Effective April 1, 2009, AB X3 3 (Chapter 18 of the Third Extraordinary Session, signed by Governor Schwarzenegger on February 20, 2009) temporarily increased the state sales and use tax rate by 1 percent. The combined state and local (Bradley-Burns local tax) tax rate, effective April 1, 2009,

Generally, district tax rates are imposed at a rate of 0.25 percent or 0.25 percent increments up to the 2 percent limit. Currently, the district tax rates vary from 0.10<sup>2</sup> percent to 1 percent. The combined state, local, and district tax rates range from 8.375 percent to 10.25 percent, with the exception of the cities of South Gate and Pico Rivera (10.75%) in Los Angeles County<sup>3</sup>.

Some cities and counties have more than one district tax in effect, while others have none. A listing of the district taxes, rates, and effective dates is available on the BOE's website: [www.boe.ca.gov/sutax/pdf/districtratelist.pdf](http://www.boe.ca.gov/sutax/pdf/districtratelist.pdf).

#### LEGISLATIVE HISTORY

Similar bills have been introduced during the last three Legislative Sessions:

- AB 978 (Perez), introduced in the 2009-10 Legislative Session, would have authorized cities and counties, subject to two-thirds approval of the voters, to impose a transactions and use tax at a rate of 0.125 percent for funding of economic development projects. This bill was never heard in a Committee.
- AB 1646 (DeSaulnier), introduced in the 2007-08 Legislative Session, would have authorized counties, subject to two-thirds approval of the voters, to impose a transactions and use tax at a rate in 0.25 percent increments and not to exceed a maximum tax rate of 1 percent for county health purposes. This bill also provided that the tax is not subject to the 2 percent rate limitation. This bill was held in the Senate Revenue and Taxation Committee.
- SB 264 (Alquist), Chapter 430, Statutes 2007, authorized the Santa Clara Valley Transportation Authority, subject to two-thirds approval of the voters of the County of Santa Clara, to impose a transactions and use tax at a rate of 0.125 percent for transit facilities and services.

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increased from 7.25 percent to 8.25 percent. The 1 percent tax rate increase will expire on either July 1, 2011.

<sup>2</sup>Some cities and counties are authorized by special legislation to impose a district tax at a rate other than a 0.25 percent. For example, the Fresno County Zoo Authority imposes a district tax at a rate of 0.10 percent.

<sup>3</sup>In 2003, SB 314 (Ch. 785, Murray) authorized the Los Angeles County Metropolitan Transportation Authority to impose a 0.50 district tax for specific transportation projects, and excluded that 0.50 percent tax from the 2 percent limitation. In 2009, voters within Los Angeles County approved an additional 0.50 percent effective July 1, 2009. The 0.50 percent tax increase in Los Angeles County raised the tax rate in the cities of South Gate and Pico Rivera from 10.25 to 10.75 percent.

- SB 203 (Simitian), Chapter 682, Statutes 2005, authorized the County of San Mateo, subject to two-thirds approval of the voters in the county, to impose a transactions and use tax at a rate of 0.125 or 0.25 percent for park and recreation purposes.

## COMMENTS

1. **Sponsor and Purpose.** This bill is sponsored by the County of Marin. According to the author's office, the purpose of the bill is to allow cities and counties to seek voter approval of additional district taxes in smaller 0.125% increments. Further, this bill will allow local jurisdictions to propose smaller taxes to fund services such as police, fire, schools, local transportation projects, parks, and libraries.
2. **BOE's costs to administer a rate of 0.125% as a percentage of revenue will be higher.** The BOE's administrative costs are driven by the workload involved in registering taxpayers, processing returns and payments, and performing audit and collection activities. These costs are relatively fixed. The cost of administering the tax is not related to the revenue generated by the tax. However, the ratio of such costs to the amount of revenue generated by the tax varies inversely with the tax rate. Therefore, if the tax rate or volume of taxable sales is very low, the ratio of cost to revenue will be high.

To illustrate this point, assume that a local jurisdiction receives \$100 in taxable sales. Let us also assume that the BOE's costs to administer \$100 in taxable sales is \$0.01. If a jurisdiction levied a tax at a rate of 0.25%, the amount of revenue generated from 0.25% tax would be \$0.25 ( $\$100 \times 0.25\%$ ). The jurisdiction's net revenue would be \$0.24 ( $\$0.25 - \$0.01$ ). If the same jurisdiction levied a tax at a rate of 0.125%, the amount of revenue generated from 0.125% tax would be \$0.13 ( $\$100 \times 0.125\%$ ). However, the jurisdiction's net revenue would be \$0.12 ( $\$0.13 - \$0.01$ ). Thus, the net revenue from imposing a tax at a rate of 0.25% versus imposing a tax at a rate of 0.125% is cut in half. Because the BOE's administrative costs are primarily fixed, the workload associated with administering a tax rate of 0.125% is essentially the same as administering the 0.25% rate. This means that the BOE's cost to administer a smaller rate as a percentage of revenue will be higher. (The administration rate of \$0.01 used above is for illustration purposes only. It does not reflect the actual costs to administer a district tax.)

3. **Though not unique, imposition of an 0.125 percent tax rate is uncommon.** Under the Transactions and Use Tax Law, counties are authorized to impose transactions and use taxes for general or special purposes at a rate of 0.25 percent, or multiples of 0.25 percent, subject to voter approval. With the exception of Section 7286.59 that authorizes counties to impose a tax at a rate of 0.125 or 0.25 percent for library purposes, counties impose transactions and use taxes at a rate of 0.25 percent, or multiples of 0.25 percent.

Currently, there are four counties that levy a library purposes tax at a rate of 0.125 percent (Fresno, Nevada, Solano, and Stanislaus).

4. **Related legislation.** AB 1086 (Wieckowski) would authorize any local government entity in the County of Alameda to impose a transactions and use tax, in excess of the combined rate limitation (2%) of transactions and use taxes imposed within a county, to support countywide transportation programs, as specified.

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**COST ESTIMATE**

This bill does not increase administrative costs to the BOE because it only authorizes cities and counties to impose a tax. However, if a city or county adopted an ordinance, they would be required to contract with and pay the BOE for all the BOE's preparation and actual administration costs associated with the new tax.

**Preparatory costs.** Based on the BOE's experience with city and county imposed taxes, the one-time preparatory costs typically can range from \$12,000 to \$138,000. Preparatory costs are the actual costs to update publications and returns, perform programming for data processing, develop instructions for both BOE staff and taxpayers, and notify taxpayers, and other necessary costs which include costs from other state agencies (e.g., California Department of Motor Vehicles costs to train staff and program computers). In addition, various factors can have an impact on the BOE's preparatory costs. For example, the BOE mails a special notice to taxpayers in the affected city or county, including adjacent areas. If a city or county borders jurisdictions with a large number of seller's permits, the BOE's mailing costs could be substantially higher.

In addition, because of certain fixed costs, the preparatory costs can vary depending on the number of new district taxes being implemented at the same time. For example, the cost of updating a publication and return to add four new taxes is similar to the cost to add one new tax. Moreover, those costs would be shared among four new districts versus one district. Thus, depending on the number of district taxes being implemented at the same time, the preparatory costs can vary.

**On-going administrative costs.** As a point of perspective, the BOE's estimated 2008-09 administrative costs assessed to the existing county special taxing jurisdictions range from \$19,000 to \$2,695,000, with the exception of Los Angeles County (Los Angeles County has a substantial higher number of sellers permits and, consequently, their administrative costs are higher than other jurisdictions).

With regard to cities, the BOE's estimated 2008-09 administrative costs assessed to the existing city special taxing jurisdictions range from \$500 to \$188,000.

The estimated assessments were determined based on the current costing model.

The proposed tax would be imposed at a rate of 0.125 percent or increments of 0.125 percent. Even though the proposed rate of 0.125 percent is less than other rates, such as 0.25 or 0.50 percent, the BOE anticipates that the costs to administer the 0.125 tax would be approximately the same as the cost to administer other taxes, such as 0.25 or 0.50 percent tax. The reason is that the workload associated with administering the proposed 0.125 percent rate is essentially the same as administering a 0.25 or 0.50 percent rate.

**REVENUE ESTIMATE****BACKGROUND, METHODOLOGY, AND ASSUMPTIONS**

For fiscal year 2009-10, there were an estimated \$492 billion in statewide taxable sales.

The Department of Finance's (DOF) current revenue forecast assumes that taxable sales increased by 4 percent for FY 2009-10. DOF further projects that taxable sales will increase 7.1% in FY 2010-11, 8% in FY 2011-12, 7% in FY 2012-13, and 6% in FY 2013-14. Based on DOF forecasts, we estimate statewide taxable sales to be \$616 billion for FY 2012-13, and \$654 billion for FY 2013-14.

**REVENUE SUMMARY**

This bill as written does not create additional revenues; however, if all special taxing jurisdictions statewide were to obtain voter approval to increase rates by 0.125 percent we estimate the revenues would be as follows:

- FY 2012-13  
The revenue impact for imposing a 0.125 percent tax on all special taxing jurisdictions would be \$770 million (\$616 billion X 0.125%).
- FY 2013-14  
The revenue impact for imposing a 0.125 percent tax on all special taxing jurisdictions would be \$818 million (\$654 billion X 0.125%).

Analysis prepared by:	Debra Waltz	916-324-1890	03/28/11
Revenue estimate by:	Lisa Buchanan	916-445-0840	
Contact:	Margaret S. Shedd	916-322-2376	
ls			0686ab030911dw.doc